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April 16, 2004

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Dear Ms. Johnson:

This letter is written in response to the request for comments on the request for burden reduction recommendations on consumer protection lending-related rules (Docket Number R-1180) under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA) review.

The first regulation for which we would like to comment relates to Loans in Identified Flood Hazard Areas. While this regulation still provides a useful purpose, we believe that the documentation requirements are burdensome and could be reduced. The requirement to obtain a record of receipt of the notice to the customer indicating that the property lies within a special flood hazard area seems unnecessary. The underlying flood insurance statute does not appear to require a record of receipt of the notice by the customer. Since an institution must obtain flood insurance prior to making the loan, it would seem that as long as the institution has evidence that the notice was delivered to the customer and that flood insurance in place, then the requirements of the law have been met. It is unnecessary to require the institution to follow up to ensure that a signed receipt is obtained for the file.

Another level of flood documentation requirements that could be reduced relates to the requirement to show evidence of coverage for the entire life of a loan. While we understand the importance of maintaining insurance for the life of a loan and for following proper procedures in the event of a coverage lapse, it seems unnecessary to maintain outdated insurance declaration forms in file to show coverage has been in place for the entire term of the loan. This is especially true on loans that have been outstanding for lengthy periods of time. As long as the bank can demonstrate flood insurance was in place at origination, that flood insurance is currently in force, and that the institution has adequate processes and procedures to follow up in the event of a lapse, it seems unnecessary to require the institution to maintain the excess documentation.

The last item related to flood regulations for which we would like to comment is that we believe there should be more explicit guidance on determining adequate flood insurance coverage for individual condominium units. It seems to take an inordinate amount of time trying to determine whether coverage is adequate. There are many complexities in determining whether association coverage is adequate on a per unit basis, whether the association or insurance agent has updated the valuation of the project timely, whether a co-insurance penalty is applicable, or whether supplemental unit insurance is needed or available. It is further complicated when the property is mixed-use, containing both residential and commercial condominium units. We recently had a situation where one of our banks contacted the NFIP Direct Writing unit and was told that supplemental insurance was available for a residential unit in a mixed-use project. This was also confirmed by an insurance agent. However, the application was subsequently rejected by that same department stating that supplemental coverage was not available for the residential unit. If employees at the NFIP give conflicting information, then how is a financial institution supposed to adequately address the coverage issue? This takes additional time and effort to document files and also creates customer relation problems.

The second regulation for which we would like to comment relates to Unfair or Deceptive Acts or Practices. Although it could be argued that many of the provisions are outdated, the majority of this regulation continues to make sense and does not impose a substantial burden on financial institutions. However, the area related to co-signers could be updated to reduce burden. Under the existing regulation, transactions involving the purchase of real property are excluded from the co-signer provisions. Refinancing of purchase transactions are also excluded from the provisions if the majority of the proceeds are used to refinance the original purchase debt. It would seem that any loan in which the lender takes a first lien position in real property as part of a mortgage transaction should be exempt from the co-signer provisions.

Given the growth in mortgage volume over the years, this loan type has become a valuable financing vehicle for more than just purchase money transactions. Borrowers have generally refinanced their mortgages more than one time over the past several years. Reviewing each refinance transaction to ensure that it is primarily refinancing purchase money is becoming more burdensome. Mortgage loans are generally lower risk transactions, and the collateral is usually sufficient to extinguish the debt in the event of default. Mortgage insurance also reduces the risk of a deficiency in the event of foreclosure. Most transactions involve family members guaranteeing the loan, and they are aware of the terms of the transaction. For these reasons, the guidance should be updated to exempt all first mortgage transactions from the requirements.

The next regulation for which we would like to comment is the Home Mortgage Disclosure Act. The requirements for obtaining and reporting information continue to grow, and this regulation is one of the most burdensome for financial institutions. With time spent training personnel, identifying covered applications, collecting monitoring information, reporting and reviewing information, and the cost of software, we conservatively estimate that our organization spends

$500,000 per year complying with this regulation. This equates to roughly $80 per HMDA application for the most recent reporting year. This cost is passed on to borrowers in the form of higher rates and fees.

Understanding the public policy factors driving the purpose behind the regulation, we still believe that the burden of collection and reporting outweighs the benefits derived from the information. This is especially true for smaller organizations. The information is to be used as a tool by the regulatory agencies in fair lending enforcement. We have been informed by the regulatory agencies that for smaller institutions, there are not a sufficient number of applications from which to pull a valid sample. Therefore, they usually need to conduct fair lending reviews on different loan types that aren't covered by HMDA. It would seem that any efficiency that could have been gained through an off-site preliminary review of HMDA data has not been realized when examining smaller institutions. Given the relatively few fair lending enforcement actions in recent years, it appears that data collection and reporting, including the most recent increase in reporting requirements, may not be as necessary as it once was.

In order to balance the public policy needs driving the regulation with the goal of reducing unnecessary burden on financial institutions, we would propose raising the asset level threshold for coverage to $500 million for regulated financial institutions. This would require a statutory change, because even with indexing, the asset threshold in the statute is significantly outdated. It has not taken into account the changes in banking and branching laws over the years or the consolidation of the banking industry. The $500 million threshold is the same as the threshold for the large institution test under the proposed revisions to the CRA regulations. This would make the two regulations consistent, and consistency eases the compliance burden. In addition, larger institutions generally have a sufficient number of applications from which the regulatory agencies could conduct preliminary off-site reviews and pull a valid sample. Smaller institutions would still be subject to the collection and retention of monitoring information pursuant to the requirements of Federal Reserve's Regulation B. This would decrease the reporting requirements for small institutions while not impacting the ability of the regulatory agencies to carry out enforcement of the fair lending laws.

An alternative solution that would help reduce some of the burden is to eliminate reporting of certain expanded information for smaller institutions. The information on rate spread, HOEPA status, and manufactured housing only provides meaningful insight from a reporting perspective if the lender engages in a high volume of transactions. As stated previously, the smaller institutions do not have a significant volume of applications from which to pull a valid sample. The additional information reporting requirements seems to only add to the burden on small institutions without providing any tangible benefit. The regulations could be amended, without statutory change, to reflect a tiered approach to detailed information reporting. Under our proposed threshold, only the institutions with assets in excess of $500 million would need to provide the additional detail as part of the reporting process. The smaller institutions would not need to report the information, thereby reducing some of the burden.

The most frequent complaint about this regulation that we receive from customers relates to the collection of race, ethnicity, and gender information. These customers feel that requesting the information is an intrusion into their privacy, despite the fact that provision of the information is entirely optional. Our lending personnel also do not feel comfortable “assigning” race and ethnicity categories to applicants when the applicants decline to provide the information. This is especially true for the recent changes creating an ethnicity category. While we understand that the change was intended to bring conformance between the categories and the census data, it has added burden to the collection and reporting requirements of the regulation.

The telephone collection of monitoring information has also added to the burden on financial institutions. We realize that there has been a significant increase in the number of applications taken over the telephone. However, providing the disclosure and requesting the information over the phone lengthens the application process and places a negative connotation on what we try to make a pleasant experience and an efficient process. The most common complaint again is that customers feel the request is an intrusion into their privacy. Instead of collecting the information over the telephone, perhaps the regulation could be amended to allow an institution to send a written request with the appropriate disclosure along with other required lending disclosures. For example, the HMDA request and disclosure could be mailed along with the good faith estimate for consumer transactions.

The final regulation for which we would like to comment is Truth in Lending. This regulation also imposes substantial burden on financial institutions. However, we still believe that the fundamental purpose of the regulation remains valid and the basic requirements imposed are still relevant in the current financial services environment. We also believe that there are requirements imposed that could be amended to reduce the burden and other amendments that would level the playing field with lenders that are not as highly regulated.

One of the main areas under the regulation that we believe should be revised relates to the rescission provisions. Rescission is one area that generates the most complaints from customers. Even though it provides protection, they generally do not understand why there is a waiting period before being allowed access to the funds. Our experience is that very few consumers rescind their transactions. We believe that the rescission provisions do provide protection to consumers and should not be eliminated entirely, especially for high cost mortgage transactions. However, we believe that certain transactions should be exempt from the requirements. We do not believe that any of the changes we propose would require statutory amendments.

The first type of transaction where rescission should be eliminated is bridge financing. We often have customers that are purchasing a new primary residence and utilize bridge financing on their existing homes for all or part of the financing. Under the regulation, the purchase financing is exempt from the requirements, as it is a residential mortgage transaction. However, the security interest taken in the existing residence triggers the rescission requirements. This creates a customer relations issue as the bank must effectively consummate the bridge financing transaction in advance of the real estate purchase transaction in order to have the proceeds available for the purchase. It can also create questions of security interest perfection, because in a true bridge loan, the lender takes a lien in both the existing residence and the new residence. By consummating the bridge loan prior to the real estate purchase transaction, the borrowers execute a security interest in a property to which they have not yet taken title. It is filed after transfer of title, but the date of execution could create issues related to priority of competing interests.

The purpose of the rescission period is to provide the borrowers with a cooling off period to review the transaction terms and determine if they would like to put their primary residence at risk as part of the transaction. Individuals are not afforded a cooling off period in purchase transactions, as the borrower generally receives advance disclosures and title to the property transfers at settlement. Once the purchase transaction is consummated, the new property becomes the primary residence of the consumer, and the consumer cannot rescind the purchase of the property. In bridge financing, the fact that a security interest is taken in the former residence is irrelevant, as the new property is the primary residence. Requiring a rescission period in this circumstance provides no real protection to the consumer and only hinders the lending process by creating two different settlements for the same transaction. The statute also does not require rescission in this circumstance. Therefore, a security interest taken in an existing residence as part of bridge financing should be excluded from the rescission requirements.

We also believe that the Board should use its authority under the statute to exempt transactions involving more sophisticated borrowers from the rescission requirements. This authority is granted at 15 USC 1604 (f). Sophisticated borrowers generally do not need the additional protections afforded by the regulation. These borrowers fully understand the transactions in which they seek to engage and will not consummate the transaction if they do not feel the terms are acceptable. They also are fully aware of the fact that they could lose their residence in the event of default. Reaching a consensus on what constitutes a sophisticated borrower could be challenging. A sophisticated borrower could be defined as any borrower that is also an owner/operator of a business or an individual that owns multiple residences. We would propose that the Board utilize the standards noted in the statute under the waiver provisions at 15 USC 1604 (g). These standards allow for the exemption of transactions involving consumers with an annual income of more than $200,000 or have net assets in excess of $1,000,000. Even though the standards were set a number of years ago, we feel that these thresholds are still appropriate today. At a minimum, we would propose that the Board allow for the waiver of rescission by consumers meeting the criteria in accordance with the waiver provisions of the statute.

One final area related to rescission where we believe the Board should use its exemption authority involves the refinancing of transactions by a new creditor. The rescission provisions already do not apply to a refinancing or consolidation of existing credit by the same creditor provided no new money is advanced as part of the transaction. We believe the same provisions should apply to a refinancing by a new creditor, as long as no new money is being advanced. Borrowers generally only refinance transactions without obtaining an advancement of additional funds when it is to their benefit. If it is a fixed rate transaction, the borrower will know the terms prior to and at consummation. For variable rate transactions, the borrower will receive advance disclosure of the variable rate terms at application and have the opportunity to review them prior to consummation. If the loan is also subject to RESPA, the creditor must also provide a good faith estimate of closing costs within three business days of application, so the borrower will know all of the fees associated with the transaction. The fact that a new creditor is involved should be irrelevant as to whether or not rescission applies. At a minimum, we would encourage the Board to adopt this provision for all mortgage transactions in which the lender takes a first lien position.

A minor revision that could be made to the regulation relates to the provision of variable rate disclosures at the time of application. 12 CFR 226.19 (b) requires that a creditor provide variable rate disclosures at the time an application form is provided to the customer. While the statute requires that open-end home equity plan information be provided with an application form, the same provision does not apply to these closed-end credit transactions. The statute merely states that the disclosures be provided at application. There are many different types of variable rate transactions, and customers do not necessarily know which program they want at the time an application form is provided to them. It would seem appropriate for the creditor to be allowed to deliver the disclosures within three business days after receiving a written application or before the consumer pays a non-refundable fee, whichever is earlier. This would bring consistency among the disclosures requirements for closed-end credit and allow the creditor to deliver the information with other required disclosures, which reduces burden. It also could lead to more meaningful disclosures, as the creditor could choose to deliver the disclosure specific to the terms selected by the consumer at application as opposed to delivering information on all of the programs offered by the creditor.

The biggest competitive disadvantage our organization faces related to this regulation is that other lending organizations do not comply with the early disclosure, advertising, or oral disclosure of APR requirements. These competitors are typically mortgage lending companies where licensing is non-existent and enforcement is extremely limited. Rates in the mortgage industry are typically not quoted as an Annual Percentage Rate. Instead they are quoted as simple interest rates and points. Customers understand this method of quoting rates and are often confused by the statement of an APR. For example, if we quote a customer a simple rate of 5.5% with a one percent origination fee and APR of 5.715%, the non-regulated lender is only quoting 5.5% with a one point origination fee for the exact same transaction terms.

It appears to the customer that they will be paying a higher rate by going through our organization. The fact of the matter is that the customer primarily cares about the interest rate and fees paid, and it is not possible to compare APR's when not all lending organizations are quoting the APR. Even quoting an APR for a sample transaction may not be relevant to the customer's specific circumstance. Therefore, we would propose that the Board use its exemption authority to exclude mortgage transactions from the oral disclosure requirements of the regulation. This would negate the need for the financial institution to maintain APR's for sample transactions, thereby reducing some of the burden.

Certain types of advertisements should also be excluded from all of the advertising requirements. For example, triggering terms in a television advertisement usually result in the addition of "fine print." This print cannot typically be read by a consumer prior to the time the advertisement is finished. It would seem that the provision of a phone number to contact the creditor for details would suffice for compliance with the advertising provisions. Lending companies that are not as highly regulated do not comply with the advertising requirements. The Board could revise the rules to bring them in conformance with other advertising regulations. For example, Federal Reserve's Regulation DD, which implements the Truth in Savings Act, provides for exclusion of certain disclosures in conjunction with radio or television advertising. We believe that it would be appropriate to include similar exclusions in the Truth in Lending regulation. This would not require any statutory changes.

Thank you for taking our comments into consideration. If you have any questions, please contact David Kelly at (303)235-1491.

Sincerely,

John A. Ikard
President

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cc: Federal Deposit Insurance Corporation